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 RUEHJI/AMEMBASSY JIDDA PRIORITY 0000
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 RUEHOS/AMEMBASSY LAGOS PRIORITY 0000
 RUFHLC/AMEMBASSY LIBREVILLE PRIORITY 0000
 RUEHEG/AMEMBASSY CAIRO PRIORITY 0000
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E.O. 12356: DECL: OADR
 TAGS: EPET, ENRG, OPEC
 SUBJECT: DISCUSSION ON WORLD OIL MARKET WITH OPEC
 DEPUTY SEC GEN FADHIL AL-CHALABI

REF: VIENNA 01636

1. C - ENTIRE TEXT
2. OPEC DEPUTY SECRETARY GENERAL MET WITH DEPUTY ASSISTANT SECRETARY OF STATE FOR ENERGY AND RESOURCES POLICY E. ALLAN WENDT FEBRUARY 23 FOR INFORMAL DISCUSSION ON WORLD OIL MARKET. REPS FROM TREASURY DEPT., S/P, NEA AND INR SAT IN.
3. AL-CHALABI OPENED BY SAYING HE WELCOMED THE OPPORTUNITY FOR THIS TYPE OF DISCUSSION. ONE OF THE PROBLEMS IN THE PAST TEN YEARS HAD BEEN THE "ABSOLUTE LACK" OF SUCH CONTACTS, ALTHOUGH FORA SUCH AS THE OXFORD ENERGY SEMINAR WERE VERY USEFUL. WENDT AGREED THAT GENERAL ENERGY EXPERT MEETINGS SUCH AS THE OXFORD ENERGY SEMINAR HAVE BEEN USEFUL AND THEN TOOK THE OPPORTUNITY TO EXPLAIN THE U.S. POSITION ON PRODUCER-CONSUMER DIALOGUE, SAYING WE WERE OPPOSED TO SPECIALLY CALLED MULTILATERAL FORA, WHICH WERE LIKELY TO FOCUS ON PRICE AND PRODUCTION -- SUBJECTS BEST LEFT TO THE MARKET PLACE -- AND BECOME POLITICIZED AND EVEN COUNTER-PRODUCTIVE. HE NOTED THAT LEADING OPEC COUNTRIES, PARTICULARLY SAUDI ARABIA, ALSO SEEMED HESITANT. WE, OF COURSE, CONTINUE TO BE IN CLOSE

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BILATERAL CONTACT WITH MOST PRODUCING COUNTRIES AND ATTEND INFORMAL ENERGY CONFERENCES SUCH AS THE OXFORD SEMINAR. AL-CHALABI RESPONDED THAT OPEC MEMBERS GENERALLY FAVORED SOME KIND OF MULTILATERAL EXCHANGE BUT DISAGREED ON THE DETAILS. THIS MADE A FORMAL DIALOGUE IMPOSSIBLE. HE WELCOMED WENDT'S EXPLANATION, BECAUSE, HE SAID, IN OPEC THEY HAD THE IMPRESSION THE U.S. OPPOSED ALL "DIALOGUE AND MULTILATERAL NEGOTIATIONS." WENDT SAID WE DID IN FACT OPPOSE MULTILATERAL DIALOGUE AND NEGOTIATIONS. OUR EXPERIENCE AT CIEC WAS FORMATIVE IN THIS RESPECT. AL-CHALABI AGREED THAT CIEC'S SCOPE WAS "TOO BROAD" (I.E., ENCOMPASSING TOO MANY NON-ENERGY ISSUES) TO ACHIEVE ANYTHING.

4. AL-CHALABI WAS ASKED WHAT A MULTILATERAL DIALOGUE WOULD COVER AND WHAT GAIN COULD POSSIBLY COME OF IT, GIVEN THAT THE U.S., AMONG OTHERS, WOULD BE INCAPABLE OF "DELIVERING" ON ANY COMMITMENTS IT MIGHT BE PRESSED TO MAKE. HE RESPONDED THAT IT WOULD BE DIFFICULT TO DEFINE THE GOALS OF A DIALOGUE. IN THE WAKE OF THE EVENTS OF THE PAST TEN YEARS, HOWEVER, HE THOUGHT BOTH PRODUCERS AND CONSUMERS HAD AN INTEREST IN STABILITY OF PRICES, SUPPLIES AND MARKET "STRUCTURE." THIS COMMON INTEREST COULD FORM THE BASIS FOR A DIALOGUE. WHAT WOULD HAPPEN IF PRICES FELL, A DEPTOFF ASKED. WENDT POINTED OUT THAT WE CLEARLY BENEFITTED FROM LOWER OIL PRICES, AS WE MADE CLEAR LAST YEAR. HOWEVER, WE ALSO CLEARLY HAD OTHER ENERGY SECURITY GOALS TO CONSIDER, NOTABLY THE NEED TO FOSTER DOMESTIC PRODUCTION. WE COULD IMPOSE AN IMPORT FEE, BUT THIS RAN COUNTER TO OUR FREE MARKET PHILOSOPHY. OUR BASIC POLICY REGARDING PRICES WAS TO RELY ON THE MARKET.

5. AL-CHALABI SAID THE MAJOR ISSUE FOR OPEC COUNTRIES NOW WAS OIL DEMAND GROWTH AND HOW THIS WOULD BE AFFECTED BY CONSUMER COUNTRY GOVERNMENTS. HE THUS SUGGESTED THAT "SECURITY OF DEMAND" COULD BE AN AREA FOR DIALOGUE. WENDT SAID WE DO NOT HAVE A POLICY TOWARD OPEC OIL AS SUCH, ALTHOUGH WE HAVE ATTEMPTED TO REDUCE OIL IMPORTS, AND THE MARKET HAS RESPONDED TO HIGH PRICES WITH INCREASED PRODUCTION OUTSIDE OPEC. HE ADDED THAT WE HAD REASON TO BE CONCERNED ABOUT OIL SECURITY -- WITNESS WHAT HAPPENED 10 YEARS AGO -- BUT WE RECOGNIZED THAT THE BULK OF EXCESS CAPACITY TODAY WAS IN THE GULF AND WE COULD NOT BE INDEPENDENT OF THAT SOURCE.

6. AL-CHALABI SAID 1973 WAS THE ONLY EXAMPLE OF A POLITICALLY-INSPIRED DISRUPTION. NOW, NO ONE IN OPEC WANTED AN INTERRUPTION OF SUPPLY, POLITICAL OR OTHERWISE. WHAT HAPPENED IN IRAN IN 1979 WAS "TOTALLY OUTSIDE OPEC'S CONTROL." IN FACT, OPEC MEMBERS MADE A BIG EFFORT TO COVER THE SHORTFALL. PRODUCTION ACTUALLY EXCEEDED CONSUMPTION IN THAT PERIOD, AND PRICES ROSE ONLY BECAUSE THERE WAS A NET STOCKBUILD, A DEVELOPMENT ALSO BEYOND OPEC'S CONTROL.

7. WENDT ASKED HOW OPEC COUNTRIES, LIBYA IN PARTICULAR, WOULD RESPOND TO A SUPPLY SHORTFALL TODAY. AL-CHALABI SAID LIBYA AND NIGERIA BOTH HAD ABOUT 1 MMBO IDLE CAPACITY; VENEZUELA, ABOUT 0.7 MMBO; AND INDONESIA, A "SMALL AMOUNT." BETWEEN THEM THEY COULD COVER ABOUT HALF OF A GULF SUPPLY DISRUPTION SHORTFALL. HE SAID HE KNEW OF NO "POLITICALLY MOTIVATED DECISION (BY LIBYA) TO REFRAIN FROM PRODUCING AT FULL CAPACITY" IN A FUTURE OIL CRISIS. ON THE CONTRARY, HE SAID, THERE WAS A DESIRE IN OPEC FOR CONSUMING COUNTRIES TO FEEL SECURE ABOUT THEIR OIL SUPPLIES. HE DID NOT KNOW WHETHER THERE WOULD BE AN EXPLICIT OPEC POLICY TO ENCOURAGE MAXIMUM PRODUCTION, BUT HE BELIEVED EACH COUNTRY WOULD PRODUCE AS MUCH AS

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POSSIBLE.

8. AL-CHALABI WAS ASKED WHETHER OPEC WOULD REGARD PRICE RISES CAUSED BY A DISRUPTION AS PERMANENT. AL-CHALABI DID NOT ANSWER DIRECTLY, BUT INSTEAD NOTED THAT IF THE LONG-TERM STRATEGY COMMITTEE FORMULA HAD BEEN ADOPTED WHEN PROPOSED (WHEN OIL WAS \$18/BARREL), OIL WOULD COST UNDER \$29 TODAY. HE AGREED WITH DEPTOFF'S COMMENT THAT, AS A RESULT OF CHANGES IN THE NATURE OF THE OIL MARKET, A DISRUPTION WOULD HAVE A DIFFERENT IMPACT TODAY FROM THAT OF A DECADE OR FIVE YEARS AGO. AL-CHALABI NOTED IN PARTICULAR THAT CONSUMING COUNTRIES NOW HAD MUCH LARGER STOCKS AND PRODUCING COUNTRIES WERE NOW "AWARE OF THE EFFECTS OF UNCONTROLLED PRICE FLARE-UPS." THERE STILL WAS A TENDENCY, HOWEVER, FOR COMPANIES, ACTING ON A RATIONAL COMMERCIAL BASIS, TO BUY AS MUCH AS POSSIBLE IN TIGHT MARKETS AND AS LITTLE AS POSSIBLE IN SLACK MARKETS, THUS COMPOUNDING PRICE PRESSURES IN BOTH DIRECTIONS.

9. THE DISCUSSION THEN TURNED TO THE CURRENT SITUATION IN THE GULF. WENDT SAID WE REGARDED THE DANGER OF A SUPPLY DISRUPTION AS REAL, ALTHOUGH PERHAPS AT TIMES OVER-DRAMATISED. AL-CHALABI TOOK A RELAXED VIEW, SAYING A DISRUPTION WAS NOT LIKELY TO LAST A LONG TIME AND COULD EASILY BE MET THROUGH A STOCKPILE DRAWDOWN. (HE NOTED THAT, AT ITS PEAK OF 5 MMB/D, THE DRAWDOWN IN EARLY 1983 EXCEEDED THE DRAWDOWN THAT WOULD BE NEEDED TO COVER THE NET SHORTFALL OF A MAJOR GULF DISRUPTION.) HE AGREED WITH DEPTOFF'S OBSERVATION THAT ATTACKS ON PRODUCTION AND LOADING FACILITIES IN GULF COUNTRIES WOULD BE A MORE SERIOUS MATTER THAN A SHIPPING DISRUPTION, BUT HE DOUBTED IRAN'S ABILITY TO LAUNCH SUCH ATTACKS SUCCESSFULLY. WENDT AGREED BUT DREW ATTENTION TO IRAN'S SUCCESS IN USING COMMANDO RAIDS WITHOUT REGARD FOR THE LIVES OF THE COMMANDOS.

10. WENDT ASKED ABOUT OPEC'S RESPONSE TO THE REPORTED NIGERIAN REQUEST FOR A HIGHER PRODUCTION QUOTA. AL-CHALABI SAID THAT, ALTHOUGH NO "FORMAL REQUEST" HAD COME TO OPEC, IT WAS CLEAR THE PRESENT NIGERIAN GOVERNMENT, BECAUSE OF ITS HUGE ECONOMIC PROBLEMS, BELIEVED A QUOTA ADJUSTMENT WAS NECESSARY. HE NOTED THERE WAS "FLEXIBILITY" IN THE QUOTA SYSTEM, IMPLYING THAT NIGERIA MIGHT TEMPORARILY INCREASE ITS PRODUCTION. HE WAS CONFIDENT THE MILITARY GOVERNMENT, UNLIKE ITS PREDECESSOR, WAS "STRONG ENOUGH TO STAY IN OPEC AND ABIDE BY ITS OBLIGATIONS," PARTICULARLY THE PRICE STRUCTURE. (COMMENT: AL-CHALABI'S LAST POINT MAY ALLUDE TO THE MARKETING ADVANTAGE NIGERIA HAS OVER OTHER OPEC MEMBERS, PARTICULARLY THE SAUDIS, AS A RESULT OF A FAVORABLE PRICE DIFFERENTIAL. AL-CHALABI MAY HAVE BEEN IMPLYING THAT OPEC WOULD "LOOK THE OTHER WAY" IF NIGERIA CHEATED ON ITS QUOTA, SO LONG AS IT DID NOT USE PRICE DISCOUNTS TO MARKET THE OIL. SUCH ACQUIESCENCE IS ALSO IMPLIED BY THE FACT YAMANI RECENTLY EXPRESSED HIS UNDERSTANDING FOR NIGERIA'S POSITION.)

11. AL-CHALABI WAS ASKED WHETHER AN EXTRAORDINARY OPEC CONFERENCE WAS LIKELY IN THE NEXT FEW WEEKS. HE THOUGHT IT WAS NOT. IN HIS VIEW SUCH A CONFERENCE WOULD BE CONVENED ONLY IF THE MARKET TOOK A SUBSTANTIAL DOWNTURN.

12. FREQUENTLY DURING THE CONVERSATION AL-CHALABI SAID THAT HE WAS SPEAKING PERSONALLY AND NOT AS AUTHORIZED SPOKESMAN OF OPEC.
SHULTZ

END OF MESSAGE

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